

**Charter School Facilities Program  
Proposition 51 Funding Round  
Staff Summary Report – January 2018**

<b>Applicant/Obligor:</b>	The Foundation for Hispanic Education
<b>Project School:</b>	Luis Valdez Leadership Academy
<b>CDS (County – District – School) Code:</b>	43-69427-0130856
<b>School Address/Proposed Site:</b>	1855 Lucretia Ave., San Jose, CA. 95122
<b>Type of Project:</b>	New Construction/Rehabilitation
<b>Type of Apportionment:</b>	Preliminary
<b>County:</b>	Santa Clara
<b>District in which Project is Located:</b>	East Side Union High School District
<b>Charter Authorizer:</b>	East Side Union High School District
<b>Total OPSC Project Cost:*</b>	NC: \$33,089,511 <u>Rehab: \$819,242</u> Total: \$33,908,753
<b>State Apportionment (50% Project Cost):</b>	NC: \$16,544,755 <u>Rehab: \$409,621</u> Total: \$16,954,376
<b>Lump Sum Contribution:</b>	N/A
<b>Total CSFP Financed Amount:</b>	NC: \$16,544,756 <u>Rehab: \$409,621</u> Total: \$16,954,377
<b>Length of CSFP Funding Agreement:</b>	30 Years
<b>Assumed Interest Rate:</b>	3.00%
<b>Estimated Annual CSFP Payment:</b>	NC: \$844,101 <u>Rehab: \$20,899</u> Total: \$865,000
<b>First Year of Occupancy of New Project:</b>	2019-20

*\*The amount identified as total project costs represents an estimate provided by the Office of Public School Construction for purposes of Preliminary-Apportionment financial soundness review. Final project costs will be provided at the time of Final Apportionment.*

Staff recommends that the California School Finance Authority (“Authority” or “CSFA”) Board determine that The Foundation for Hispanic Education (FHE), on behalf of Luis Valdez Leadership Academy (“LVLA” or “Luis Valdez”) is financially sound for the purposes of Charter School Facilities Program (“Program” or “CSFP”) Preliminary Apportionment. This determination as it relates to Preliminary Apportionment is in place for twelve months and assumes no financial, operational, or legal material findings within this time period. This recommendation is contingent upon LVLA having its charter petition renewed in 2018 and FHE complying with the California Enterprise Development Authority and City National Bank regarding its 2017 financing. In addition, LVLA must elect to have its CSFP payments

intercepted at the state level, pursuant to Sections 17199.4 and 17078.57(a)(1)(A) of the Education Code. Staff recommends that the Authority Board direct staff to notify the Office of Public School Construction (OPSC) and the State Allocation Board regarding this determination.

**Application Highlights:** Below, staff has highlighted key criteria that were evaluated when conducting its financial soundness review of FHE on behalf of LVLA. Detailed information is contained in the body of the report.

<b>Criteria</b>	<b>Comments</b>
<b><i>Foundation for Hispanic Education</i></b>	
Demographic Information	<ul style="list-style-type: none"> <li>• FHE has shown consistent student enrollment growth over the past three years, growing from 501 students in 2014-15 across two schools to 1,037 students in 2017-18 across three schools.</li> <li>• FHE has demonstrated average daily attendance rates over 94.5% for the past two years.</li> <li>• FHE has a combined wait list of 434 students across its three charter schools.</li> </ul>
Debt Service Coverage	FHE substantially exceeds the minimum required debt service coverage requirement with coverage levels of 339.8%, 322.7%, and 358.9% for 2020-21 through 2022-23, respectively (assuming lease revenues) and 256.0%, 238.9%, and 275.1% for the same years, respectively, (without lease revenues).
Other Financial Factors	<ul style="list-style-type: none"> <li>• FHE will not have to rely on private contributions to meet the debt service coverage requirement.</li> <li>• As of June 30, 2017, FHE had net working capital of \$2,572,185, representing 16.1% of expenditures, as well as cash and cash equivalents of \$4.0 million.</li> </ul>

<b><i>School Information, Luis Valdez Learning Academy</i></b>
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Demographic Information	<ul style="list-style-type: none"> <li>• Over the past three years, Luis Valdez has shown consistent enrollment growth, growing from 91 students in 2014-15 to 377 students in 2017-18.</li> <li>• Luis Valdez achieved ADA rates averaging 95% over the past two years and year-to-year retention rates of 95% for each of the past two years.</li> </ul>
Eligibility Criteria	Luis Valdez Leadership Academy has met all eligibility criteria: (1) LVLA began operation in 2014; (2) Luis Valdez Leadership Academy’s charter was approved in 2014 and is in place through June 2018; (3) Luis Valdez Leadership Academy is in good standing with its chartering authority, and in compliance with the terms of its charter.
Student Performance	Based on the new “Smarter Balanced” testing results for 2016-17 (only one year reported by CDE), Luis Valdez underperformed in relation to the traditional public school, Yerba Buena High School, with which it shares its campus and chartering authority, East Side Union High School District. However, FHE’s other charter school that was reviewed, Latino College, performed comparably to Yerba Buena and the District in English Language Arts, though not in mathematics. In addition, FHE submitted a corrective action plan to address Luis Valdez’s performance.

**Program Eligibility:** On October 27, 2017, at CSFA staff’s request, verification was received from East Side Union High School District (District) confirming that Luis Valdez Leadership Academy (1) is in compliance with the terms of its charter agreement and (2) is in good standing with its chartering authority. Luis Valdez Leadership Academy’s current charter is effective through June 30, 2018. It is noteworthy that the Chief Financial Officer for FHE, Michael Ramirez, has informed staff that the school submitted its charter renewal petition in December 2017 in the form required. A vote by the District board is anticipated for March 2018 and FHE expects renewal will be granted, based on the District’s approval of the charter for a sister school as well as LVLA’s good standing with the District. Because the current charter is scheduled to expire on June 30, 2018, the recommendation for financial soundness in this report is contingent upon LVLA having its charter petition renewed.

**Legal Status Questionnaire:** Staff reviewed the applicant’s responses to the questions contained in the Legal Status portion of the application. No information was disclosed that would lead staff to question the financial or legal integrity of this applicant.

**Project Description:** The Foundation for Hispanic Education is applying for new construction and rehabilitation financing for Luis Valdez Leadership Academy (LVLA). LVLA currently leases 13 portable buildings on the Yerba Buena High School campus from the East Side Union High School District. The Rehabilitation request includes like-for-like replacement of one portable classroom and the New Construction request includes

construction of 17 new classrooms. The 17 new classrooms will be housed in a 2-story, permanent school building on 1.33 acres of the Yerba Buena campus. The application also includes requests for available supplemental grants, including urban, site development, multi-level and small project, as applicable. The anticipated date of project occupancy is August 2019.

**Obligor Organizational Information:** The Foundation for Hispanic Education was established in 1981 by Dr. B Roberto Cruz with the intention of providing education and support to underserved Latino learners and leaders in the Bay Area, specifically East San Jose.

The Foundation for Hispanic Education operates The Center for Latino Education and Innovation and 3 charter high schools (grades 9-12): Latino College Preparatory Academy (LCPA), Luis Valdez Leadership Academy, and B Roberto Cruz Leadership Academy (B. Roberto Cruz). The Center for Latino Education and Innovation is a collaboration with Santa Clara University that provides a pre K-12 education pipeline for the underserved in Santa Clara County. The three charter academies, opened in 2001, 2014, and 2015, respectively, all serve Latino-dominant East San Jose and emphasize bi-literate education.

The Foundation for Hispanic Education’s mission is to provide educational leadership for English Language Learners (ELL) and the development of specialized training programs for teachers of English Language Learners by: 1) Supporting existing programs to ensure continued achievement; 2) Creating and supporting teacher training programs specifically directed at underachieving ELL students; 3) Providing information and direction in attaining sufficient financial aid to support post-secondary education admission and retention.

The Foundation for Hispanic Education is serviced by a 12 member board that includes Chairman Edward Alvarez; Vice Chairman John Sobrato; Secretary Raymond Ruiz; Dr. Ramon Jimenez; Joe Parisi; Henry Michon; Maria Schabbing; Michael Walker; Jose Iglesias; Jorge L. Escobar; Arnoldo Avalos; and Sarah Valencia.

**School Organizational Information:** Luis Valdez Leadership Academy is a public charter school located within the boundaries of the Eastside Union High School District and is authorized by the Eastside Union High School District. The school is a direct-funded independent charter school and is operated by The Foundation for Hispanic Education, a California public benefit corporation with IRS approved 501(c)(3) status. Luis Valdez Leadership Academy operates autonomously from the District, with the exception of the supervisory oversight as required by statute and other contracted services as negotiated between the District and the School. Luis Valdez commenced its operations with the 2014-15 academic year.

Luis Valdez shares the same mission statement as the other academies under FHE which is “to provide a rich, meaningful education in a nurturing environment where students are continually challenged and their natural curiosity, creativity, and talents can thrive. We are a collaborative community of educators and families working together to help our students

grow into virtuous, courageous, and intelligent citizens, equipped with a love of learning and a love of life, and eager to contribute to a better world.”

The core mission/philosophy of Luis Valdez Leadership Academy is a belief that all English Language Learner students in East San Jose can succeed in any college/university if they are prepared with a rigorous college-preparatory education, extended time for learning inside and outside the classroom, and language-acquisition support. Because almost 100% of students at Luis Valdez Leadership Academy come from working class Hispanic backgrounds, the school is prepared to deal with the unique challenges their parents, often immigrants, present, specifically: 1) Parental understanding of the academic system; 2) Educational need of parents to facilitate “letting go” of graduates into higher educational systems (colleges/universities); and 3) Distinctiveness that characterizes students: parental education.

The framework for student education at Luis Valdez Leadership Academy succeeds because it safeguards that: students and teachers spend more time in the classroom than their counterparts in other schools in the District; students focus on developing the knowledge, skills and leadership traits necessary for college and life success; students further develop those skills to become poised, articulate, confident leaders committed to giving back to the East San Jose community; teachers collaborate with other high performing public (Summit Public Schools) and private (Cristo Rey San Jose) high schools, and the East Side Union High School District, to refine, reshape, share and develop effective language-acquisition teaching strategies; the Academy’s Student Success Center and Alumni Support Program work closely with parents and guardians to teach them how to support their children through the college application process and through their college years; teachers and administrators bridge the gap between school and community by engaging in monthly service projects with students; and teachers provide students and parents 24/7 access for homework assistance and curriculum questions.

**School Academic Performance:** The following tables represent the academic performance of LVLA, the combined averages of Yerba Buena and William C. Overfelt High (Local Schools), and the District. The results are provided through CDE’s CAASPP Smarter Balanced testing data. Because LVLA begin operation in 2014, there is only academic performance data for the 2016-17 school year. Please note: there is not an “All Student Performance” measure for high schools.

**English Language Arts – Comparison**

	Years		
	2014-15	2015-16	2016-17
LVLA	N/A	N/A	34%
Local Schools	50%	48%	53%
District	61%	62%	66%

**Mathematics– Comparison**

	Years		
	2014-15	2015-16	2016-17
LVLA	N/A	N/A	6%
Local Schools	24%	30%	27%
District	39%	39%	41%

In considering the combined percentages under “Standard Exceeded” and “Standard Met,” Luis Valdez performed significantly lower than the District and the non-charter, Yerba Buena, in both English Language Arts and Mathematics. However, a sister school of LVLA, Latino College, performed comparably to both the District and Yerba Buena in English Language Arts, but still lower in mathematics. It is noteworthy that the unduplicated counts (percentages) for the compared entities are as follows: 80% for Luis Valdez; 93% for Latino College; 82% for Yerba Buena; and 53% for the District. Given Luis Valdez’s lower performance, even with comparable unduplicated counts to the non-charter, Staff requested FHE to provide an explanation and action plan to address the lower performance of Luis Valdez. Staff’s review of the action plan determined that it was reasonable and capable of addressing the issue with performance.<sup>1</sup>

Given the school’s action plan for Luis Valdez as well as Latino College’s good performance with English Language Arts, staff concludes that the academic performance of Luis Valdez should not be an impediment towards a recommendation for financial soundness.

**Enrollment Trends and Projections:** The table below presents school and enrollment information for FHE’s schools for 2014-15 through 2022-23.

District-wide Student Enrollment and Average Daily Attendance

	2014-15	2015-16	2016-17	2017-18*	2018-19	2019-20	2020-21	2021-22	2022-23
FHE Enrollment	501	696	925	1,037	1,162	1,218	1,271	1,315	1,334
ADA	95.2%	95.0%	94.1%	95.0%	95.0%	95.0%	95.0%	95.0%	95.0%

Enrollment by School

	2014-15	2015-16	2016-17	2017-18*	2018-19	2019-20	2020-21	2021-22	2022-23
LCPA	410	422	440	430	420	450	450	450	450
LVCA	91	193	295	377	392	400	421	400	400
B. Roberto Cruz	N/A	81	190	230	350	368	400	465	484

<sup>1</sup> The school’s response and action regarding Luis Valdez’s performance is available upon request.

*\*The totals in this table are based on FHE's reporting of enrollment by school. Although the total enrollment for 2017-18 used in FHE's multi-year budget projections is 1,050, staff considers the difference in totals (13 students) not to be material.*

Luis Valdez has shown consistent growth from 91 students in grade 9 in 2014-15 to 377 students in grades 9-12 in 2017-18, both from the addition of a new grade each year as well as overall increased enrollment within grades. Luis Valdez is projected to grow to 400 students during the first year of CSFP project occupancy in 2019-20. Subsequently, Luis Valdez is expected to have one year with a small increase to 421 in 2020-21 and then remain level at 400 students in all further projected years. Luis Valdez has achieved year-to-year retention rates of 95% for 2016-17 and 2017-18, as well as average daily attendance (ADA) rates of 96.4% and 94.2% for 2015-16 and 2016-17, respectively.

Enrollment for all FHE schools in-aggregate has shown consistent growth; growing from 501 students in 2014-15 to 1,037 schools in 2017-18. Enrollment growth can be attributed to the addition of new grades and expansion of students within grades. FHE is projecting overall enrollment growth to 1,315 in 2021-22 and 1,334 in 2022-23, representing growth of 28.6% over five years, or about 5.7% per year. FHE also provided supportive evidence based on student capacity of its facility projects at the shared campus for Latino College and B. Roberto Cruz. The ADA for FHE for 2015-16 and 2016-17 was 95.0% and 94.1%. Although the year-to-year retention rate for B. Roberto Cruz was relatively low at 85% and 78% for the past two years, the year-to-year retention rates for Latino College and Luis Valdez for the past two years averaged about 96%. Furthermore, FHE provided an explanation and a plan of action to address the low retention rate for B. Roberto Cruz. Finally, the number of students on the waits lists are high at 177 for Luis Valdez and 257 for the shared campus of Latino College and B. Roberto Cruz.

Overall, based on its consideration of multiple factors, including retention rates, historical enrollment, and historical ADA, staff concludes that FHE's student enrollment projections and assumed ADA (95%), as incorporated into its multi-year budget projections, are reasonable. Staff also concludes that FHE's enrollment growth, ADA, and retention rates, are supportive of a recommendation for financial soundness.

**Financial Analysis:** This financial analysis is based on the consideration and review of the following for FHE, the financial obligor and Applicant, on behalf of Luis Valdez: (1) audited financial statements for 2014-15, 2015-16 and 2016-17; (2) adopted budget for 2017-18; and (3) budget projections for 2018-19 through 2022-23 along with assumptions.

**Assumptions:** FHE's multi-year budget projections are based upon the following assumptions: (1) occupancy of the rehabilitation and new construction projects in 2019-20; (2) enrollment projections as provided above under "Enrollment Trends and Projections"; (3) ADA rates of 95%, which are consistent with historical performance; (4) Local Control Funding Formula (LCFF) per-ADA funding rate for Luis Valdez of \$11,110, \$11,779, and \$12,330 for 2017-18 through 2019-20, and comparable rates for the other two schools, which is reasonable and conservative given Luis Valdez's unduplicated count of about 80%. (5) \$725,000 per year in lease revenues stemming from FHE's owned properties; and (6) student to teacher ratios of about 25:1, on average. It is noteworthy that staff conducted its

analysis of debt service coverage both including and not including the assumption of lease revenues.

Long Term Liabilities: As set forth in the 2016-17 audited financial statements, FHE had the following long-term debt obligations as of June 30, 2017: (1) Note payable (mortgage) in the amount of \$17.0 million to City National Bank and California Enterprise Development Authority resulting from a refinance of a loan of \$15.0 million; (2) Line of credit with City National Bank in the amount of \$1,050,000; and (3) Note payable to a board member in the amount of \$ 1,730,000. Upon staff's request, FHE provided evidence that its annual obligations in interest and principal payments are incorporated into its multi-year budget projections, including evidence of incorporation of its annual payments of \$1,121,576 on its Note payable to City National Bank and California Enterprise Development Authority.

The loan payable to City National Bank and California Enterprise Development Authority covers the land and property at the Story Road campus, which houses Latino College and B. Roberto Cruz, as well as other assets of FHE unrelated to the CSFP project. It is noteworthy that this loan matures in 2027 with a balance of \$12.35 million, and that FHE plans to refinance at that time. Upon staff's request, FHE's Chief Financial Officer provided the following response to address FHE's ability to refinance in 2027:

- “1. With our current obligation, the loan to value ratio is close to 50%. When currently planned and funded (by donors) capital improvements are completed in the next 2 years, our loan to value will, at 2027, be closer to 35%. Based on our prior experience, we believe lenders will look favorably upon our application.
2. We have broad expertise, at the board and staff levels, with the mortgage market. Over the years, we've obtained New Market Tax Credits, pension funds, and tax exempt and commercial loans.
3. Our expectation is that our 3 schools, having reached programmatic maturity, will be highly effective academically and financially sound. We would have resources sufficient to reflect long term sustainability even in the event of expected downturns in state funding.
4. Our strong and positive history with lenders also contributes to our confidence in securing new financing.
5. Based on our previous experiences in the mortgage market we will also consider the traditional long term bond market as an alternative in 2027 given that we would have achieved operational maturity and are better able to commit to a long term bond.”

Private Contributions: FHE does not rely on any private contributions to demonstrate financial soundness.

**Other Considerations:** Based on the audited financial statements, in 2014-15, Laureate Education, Inc. (Laureate) pledged to donate \$5.0 million to FHE through a distribution of \$500,000 per year over 10 years. While the audited financial statements recognize the \$5.0 million pledge in 2014-15 as a revenue item, in order to show FHE’s operating performance based on its normal revenues and expenses, staff incorporated this receipt of funds in its analysis as cash inflows over 10 years rather than a one-time revenue item in 2014-15.<sup>2</sup> Because FHE recognizes lease revenues stemming from its owned properties in its multi-year projections, and these are not student related, the results for debt service coverage are given both with and without such revenues, and the results without lease revenues are given more weight in the determination of financial soundness.

**Benchmark Summary and Analysis:** The following table and summary listing sets forth the results of staff’s analysis regarding FHE’s financial soundness. Where a threshold has been established based on industry standards or practice, the listing indicates whether or not the threshold was met. Staff utilized a financial model which incorporated financial data from audited financial statements, adopted budget, and multi-year projections and that adjustments were made to specific information that is reflected in the model and table below. Specifically, the model and table reflect the receipt of \$500,000 per year in cash inflows over 10 years resulting from the \$5.0 million pledge in 2014-15 from Laureate, which is consistent with the terms of the agreement, instead of a one-time revenue item of \$5.0 million in 2014-15.

OPERATIONAL, FINANCIAL & STUDENT PERFORMANCE METRICS									
	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
<b>OPERATIONAL &amp; FINANCIAL</b>									
Enrollment	501	696	925	1,050	1,162	1,218	1,271	1,315	1,334
Average Daily Attendance (ADA)	477	661	870	998	1,104	1,157	1,207	1,249	1,267
Average Daily Attendance (%)	95.2%	95.0%	94.1%	95.0%	95.0%	95.0%	95.0%	95.0%	95.0%
LCFF Sources/ADA	\$ 9,067	\$ 10,490	\$ 11,129	\$ 11,208	\$ 11,731	\$ 12,839	\$ 12,748	\$ 12,379	\$ 12,518
% Change		15.7%	6.1%	0.7%	4.7%	9.5%	-0.7%	-2.9%	1.1%
Operating Revenues/ADA	\$ 19,762	\$ 16,869	\$ 18,262	\$ 16,099	\$ 16,296	\$ 16,877	\$ 16,721	\$ 16,233	\$ 16,390
% Change		-14.6%	8.3%	-11.8%	1.2%	3.6%	-0.9%	-2.9%	1.0%
Operating Expenses plus CSFP Lease/ADA	\$ 19,845	\$ 18,377	\$ 18,352	\$ 15,207	\$ 15,886	\$ 15,645	\$ 15,507	\$ 15,178	\$ 15,103
% Change		-7.4%	-0.1%	-17.1%	4.5%	-1.5%	-0.9%	-2.1%	-0.5%
Free Cash Flow/ADA	\$ (83)	\$ (1,508)	\$ (91)	\$ 892	\$ 410	\$ 1,233	\$ 1,214	\$ 1,055	\$ 1,287

	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
<b>DEBT SERVICE COVERAGE</b>									
Total Operating Revenues	\$ 9,423,948	\$ 11,149,452	\$ 15,887,808	\$ 16,058,586	\$ 17,988,880	\$ 19,528,625	\$ 20,190,103	\$ 20,278,505	\$ 20,770,889
Total Operating Expenses	9,463,756	12,146,442	15,966,563	15,168,911	17,536,262	18,102,430	17,859,489	18,095,493	18,274,695
Total Other Sources/Uses	(410,127)	(27,778)	(181,436)	-	-	-	-	-	-
Net Income Available for CSFP Lease Payment	(449,935)	(1,024,773)	(260,191)	889,675	452,618	1,426,195	2,330,614	2,183,012	2,496,194
Add Back Capital Outlay	-	-	-	-	-	-	-	-	-
Add Back Depreciation	-	-	-	608,574	608,574	608,574	608,574	608,574	608,574
Adjusted Net Income Available for CSFP Lease Pymt.	(449,935)	(1,024,773)	(260,191)	1,498,249	1,061,192	2,034,769	2,939,188	2,791,586	3,104,768
CSFP Lease Payments	-	-	-	-	-	-	865,000	865,000	865,000
Free Cash Flow	\$ (449,935)	\$ (1,024,773)	\$ (260,191)	\$ 1,498,249	\$ 1,061,192	\$ 2,034,769	\$ 2,074,188	\$ 1,926,586	\$ 2,239,768
DSC from Adj. Net Income	N/A	N/A	N/A	N/A	N/A	N/A	339.8%	322.7%	358.9%
DSC from LCFF Sources subject to CSFA Intercept								0.0%	0.0%
<b>LIQUIDITY</b>									
Current Assets	\$ 2,333,737	\$ 2,015,666	\$ 7,677,777						
Current Liabilities	1,601,407	2,145,431	5,105,592						
Net Working Capital	\$ 732,330	\$ (129,765)	\$ 2,572,185						
Net Working Capital/Oper. Expenses	7.7%	-1.1%	16.1%						
Unrestricted Cash & Cash Equivalents	\$ 911,937	\$ 619,249	\$ 4,020,730						
Unrest. Cash & CE/Oper. Expenses (Days)	35	19	92						
Unrest. Cash & CE/All Expenses (Days)	35	19	92						

<sup>2</sup> In actuality, FHE received \$625,000 in 2014-15, and will have received \$500,000 in eight subsequent years and \$375,000 in the final year, together adding to \$5.0 million.

Benchmark Summary:

- Free Cash Flow/ADA (average) – Met: \$490 (>\$0)
- Free Cash Flow (average) – Met: \$1.01 million (>\$0)
- Debt Service Coverage from Adjusted Net Income – 339.8%, 322.7% and 358.9%
- Net Working Capital as Portion of Operating Expenses – Met: 7.6% (>5%)
- Unrestricted Cash & Cash Equivalents as Portion of All Expenses – Not Met: 49 days (> 90 days)

Financial Performance and Special Considerations: FHE showed net deficits of \$449,935, \$1.02 million, and \$260,191 for 2014-15 through 2016-17, respectively. Based on its adopted budget and multi-year budget projections, FHE is anticipating a net gain of \$889,675 for the current 2017-18 fiscal year. Also, based on its multi-year budget projections, FHE is projecting the following net gains: \$452,000 for 2018-19; \$1.4 million for 2019-20; \$2.3 million for 2020-21; \$2.2 million for 2021-22; and \$2.5 million for 2022-23. Notwithstanding the net gains in future years, because of the net deficits during 2014-15 through 2016-17, staff requested an explanation from the FHE's Chief Financial Officer (CFO) as to the discrepancy. The CFO clarified that, because FHE opened two new charter schools in 2014-15 and 2015-16, respectively, it was faced with additional expenses associated with start-up, including additional investments in personnel, furniture, fixtures, and equipment. In addition, he indicated that Luis Valdez had a teacher-to-student ratio of 1:17 in 2017, also associated with start-up costs. Staff considers FHE's explanation regarding the shortfalls in 2014-15 through 2016-17 to be reasonable and recognizes that the anticipated enrollment growth and efficiencies gained in future years are consistent with the projected net gains.

Notwithstanding not meeting the 5% threshold for "Net Working Capital as a Portion of Expenditures" in 2015-16, FHE met the associated thresholds for 2014-15 at 7.7% and 2016-17 at 16.1% and has an average of 7.6% the past three years. As of June 30, 2017, FHE had \$4.0 million in available cash and cash equivalents. As such, staff considers FHE's liquidity to be supportive of a recommendation for financial soundness. Although FHE's average unrestricted cash and cash equivalents as portion of expenditures (over the past three years) is 49 days, on balance with other strengths, including liquidity and debt service coverage, staff does not consider this to be an impediment in its recommendation for financial soundness.

Based on the multi-year budget projections, FHE substantially exceeds the minimum required debt service coverage requirement with debt service coverage levels of 339.8%, 322.7%, and 358.9% for 2020-21 through 2022-23, respectively (assuming lease revenues) and 256.0%, 238.9%, and 275.1% for the same years, respectively (without lease revenues). It is especially noteworthy that staff stress tested the financial model assuming no lease revenues and determined that FHE could withstand a 12% reduction in its projected enrollment (about 150 students), representing an increase of only 100 students

from its current enrollment across all three charter schools, and still meet the minimum debt service coverage requirement of 100%.

Overall, staff's review the full set of financial considerations in this analysis is supportive of a recommendation of financial soundness.

**Strengths, Weaknesses and Mitigants:**

- + As of June 30, 2017, FHE had net working capital of \$2,572,185, representing 16.1% of expenditures, as well as cash and cash equivalents of \$4.0 million.
- FHE has long-term debt in the form of a note payable for \$17.0 million that will mature in 2027 with a balance of \$12.3 million.
- + FHE does not rely on private contributions.
- + FHE projects debt service coverage of 256.0%, 238.9%, and 275.1% for 2020-21, 2021-22, and 2022-23, respectively, without lease revenues, and FHE can withstand a reduction in projected enrollment of 12% in still meet the minimum required debt service coverage requirement of 100%.
- + Luis Valdez had year-to-year retention rates of 95% for each of 2016-17 and 2017-18 and average daily attendance rates that averaged 95% over the past two years.
- + FHE's combined wait list for all three charter schools is 434 students, with Luis Valdez having 177 students on its wait list, and the combined wait list for the other two schools having 257 students.
- +/- Based on the new "Smarter Balanced" testing results for 2016-17 (only one year reported by CDE), Luis Valdez underperformed in relation to the traditional public school, Yerba Buena High School, with which it shares its campus and its chartering authority, East Side Union High School District. However, FHE's other charter school that was reviewed, Latino College, performed comparably to Yerba Buena and the District in English Language Arts, though not in mathematics. In addition, FHE submitted a corrective action plan to address Luis Valdez's performance.

**Staff Recommendation:** Staff recommends that the California School Finance Authority ("Authority" or "CSFA") Board determine that The Foundation for Hispanic Education (FHE), on behalf of Luis Valdez Leadership Academy ("LVLA" or "Luis Valdez") is financially sound for the purposes of Charter School Facilities Program ("Program" or "CSFP") Preliminary Apportionment. This determination as it relates to Preliminary Apportionment is in place for twelve months and assumes no financial, operational, or legal material findings within this time period. This recommendation is contingent upon LVLA having its charter petition renewed in 2018 and FHE complying with the California Enterprise Development Authority and City National Bank regarding its 2017 financing. It is also contingent upon LVLA

electing to have its CSFP payments intercepted at the state level, pursuant to Sections 17199.4 and 17078.57(a)(1)(A) of the Education Code. Staff recommends that the Authority Board direct staff to notify the Office of Public School Construction (OPSC) and the State Allocation Board regarding this determination.